No. 12908

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

J. J. McDONELL,

Appellant,

vs.

PAUL W. SAMPSELL, Trustee of the Estate of Hacker-Byrnes Corporation, bankrupt,

Appellee.

APPELLANT'S REPLY BRIEF.

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I.

Introductory Statement.

In his Reply Brief, the Appellee has misconceived the duty of the bankruptcy court on hearings to disallow or subordinate claims of the officers or directors of a corporation for salaries. He has cited only one case which has any bearing in this connection, *Pepper v. Litton,* 308 U. S. 295. The other authorities have nothing whatsoever to do with this problem and go only to the jurisdiction and power of the Court, which appellant concedes. Appellee assumes that under no circumstances, may an officer or director recover salary against the bankrupt corporation, which is wholly fallacious. The instant brief will expose these fallacious contentions, which the Appellee finds he must urge to support the erroneous decision of the District Court.

II.

Summary of the Argument.

A. The Appellee wholly disregards the fact that the Appellant came to the bankrupt corporation as a stranger and purely as an employee, without any financial interest whatsoever therein.

B. The Appellee wholly disregards the fact that Appellant was not an officer or director of the bankrupt corporation for more than six months prior to its insolvency and makes statements of the financial condition of the corporation during the time of his directorship, which is wholly unsupported by any evidence in the transcript.

C. The Appellee wholly disregards the fact that the salary agreed to be paid to the Appellant was fair and reasonable.

III.
ARGUMENT.

A. The Appellee Wholly Disregards the Fact That the Appellant Came to the Bankrupt Corporation as a Stranger and Purely as an Employee, Without Any Financial Interest Whatsoever Therein.

The Appellee finds no fault with the decision in the case of *Pepper v. Litton, supra,* which apparently the Appellee wholly relies on by citing large portions thereof. However, it is curious to note that he has not cited any facts upon which said case is based. This case arose out of a claim made by the dominant stockholder of a corporation for back wages, which claim was a "planned and fraudulent scheme" and was disallowed entirely by the court. We wish to emphasize this because in the present case, the contract was found to be legal and enforceable, but payment thereof was subordinated to other creditors.

Appellant maintains that the aforesaid case supports our contention and as it states: "the essence of the test is whether or not under all the circumstances, the transaction carried the earmarks of an arms-length bargain." Did not this appellant come to the bankrupt corporation and deal with it at arms-length? We cannot conceive how Appellee can argue that he did not. The undisputed facts are that he was a stranger who was employed by the bankrupt corporation at a designated salary. Does Appellee maintain that this is fraudulent and that a prospective employee must look into the financial affairs of a

corporation before he becomes employed by it, to ascertain whether or not it can pay the salary, as a pre-requisite to enforcing a claim for wages thereafter, if the same is not paid?

Appellee has also entirely disregarded the fact that there was no fraud involved in the making of the employment contracts in question. In this connection, Appellee also disregards the case: *In re American Range and Foundry,* 22 F. 2d 558, the facts of which, insofar as any fiduciary relationship are concerned, are much stronger than in the present case, for the reason that it involved a claim for wages on a contract for services by a director, who, with his son, were the sole stockholders of the corporation. The claim was upheld and approved by the court. Appellee has made no answer to this case, while quoting generally the law of fiduciary relationship. We have pointed out in our Opening Brief, that the Appellant had no financial interest in the bankrupt corporation and that he was purely a "dummy" director, which is answered by Appellee at page 10 of his Reply Brief, with the absurd argument that "no one forced him to accept the position as an officer or director." The undisputed evidence is that he was merely appointed by Raymond Hacker, the sole owner of the corporation.

B. The Appellee Wholly Disregards the Fact That Appellant Was Not an Officer or Director of the Bankrupt Corporation for More Than Six Months Prior to Its Insolvency and Makes Statements of the Financial Condition of the Corporation During the Time of His Directorship, Which Is Wholly Unsupported by Any Evidence in the Transcript.

There was no testimony at the time of the hearing on this claim, that the bankrupt corporation was insolvent during the time the Appellant was an officer or director thereof. There is no mention of insolvency in the transcript. It appears that the corporation was operating with a shortage of working capital during said times; this is a far cry from insolvency. From such a situation, it is certainly illogical to even imply insolvency. Furthermore, in any event, there is nothing in this situation which could in any manner even create an implication that any action or conduct on the part of the Appellant contributed to the bankruptcy of this corporation. If the Trustee, the Appellee herein, would be fair in this matter, he would advise the Court that the bankruptcy was caused by the withdrawal of capital and inventory by the new parties who came into the corporation in the middle of 1948.

In Argument I of his Reply Brief, commencing at page 7, Appellee has quoted, *haec verba,* the Conclusions of Law which are set forth in the transcript [Tr. pp. 30-32]. We reiterate that from a reading of them, it cannot be conceived how or in what manner they are conclusions of law, as the same are based wholly upon a supposition that if certain things had been done during 1948, other things might have happened.

C. The Appellee Wholly Disregards the Fact That the Salary Agreed to Be Paid to the Appellant Was Fair and Reasonable.

That nowhere in Appellee's Reply Brief, is there any statement or argument that the guaranteed salary agreed to be paid to Appellant was not a fair and reasonable salary. He endeavors, by argument at page 14 of his Reply Brief, to designate the payment of such salary, "an optimistic plan" and entirely ignores the fact that new capital was supposed to have been brought into the corporation by Messrs. Sommers, Boyer and Kaplan [Tr. p. 71] and that these parties insisted in the middle of 1948 that he stay on, when he attempted to resign, which certainly prevented him from going out and earning a salary which he was entitled to, considering his experience.

The Appellee endeavors to becloud the issue here by setting up in Argument III of his Reply Brief, commencing at page 11, a description of salaries agreed to be paid to other employees. This is wholly irrelevant because we are not concerned with what other employees were agreed to be paid. Appellee has failed to advise the court that these other employees had been with the bankrupt corporation for long periods of time at certain fixed salaries, whereas, the Appellant only came to the corporation as a stranger late in 1947 with 25 years of experience and background in the floor covering business, where he had earned a salary equal to that agreed to be paid to him by the bankrupt corporation. As we have stated in our Opening Brief, just because the corporation was unsuccessful, is no reason for penalizing an officer

or director by subordinating his claim to those of other creditors.

Barlow v. Budge, 127 F. 2d 440.

Appellee has also made no reply to the statement of law contained in this case.

IV.
Conclusion.

From a reading of the Statements of Fact set up by both the Appellant and Appellee, the Court can conclude that there is no apparent disagreement of the parties as to the facts in this case. The doctrine advanced by the Appellee is untenable for the reason that if it were the law, no director or officer could ever recover back salary from a bankrupt corporation. This is clearly not the holding in all of the authorities cited by both parties. The result of the order appealed from is not only harsh, but the order itself is a violation of clear and positive rules of law, which should be properly applied to the undisputed facts in this case.

The Order appealed from should be reversed.

Respectfully submitted,

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